



**U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT**  
WASHINGTON, DC 20410-0500

OFFICE OF HOUSING

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<b>Special Attention of:</b>	<b>Notice:</b>	<b>H 2021-02</b>
Multifamily Regional Directors, Multifamily Division Directors for Production and Asset Management, Multifamily Asset Management Staff, Property Owners, and HUD-Approved Mortgagees	Issued:	June 30, 2021
	Expires:	This Notice remains in effect until amended, revoked, or superseded
	Supersedes:	Notice H 2012-10 and Appendix C of the Mark-to- Market Operating Procedures Guide

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**TITLE**

Guidelines for Certain HUD Approvals Regarding Properties Encumbered by HUD-Held Mark-to-Market Program Debt and Portfolio Reengineering Demonstration Program Debt

**SUBJECT**

This Notice addresses the assumption, subordination, or assignment of Mark-to-Market Program (“M2M”) loans and Portfolio Reengineering Demonstration Program (“Demo Program”) loans in transfer or refinance transactions; actions in the event of default upon maturity of such loans; and requests to transfer budget authority of a project-based Section 8 Housing Assistance Payments Contract under Section 8(bb)(1) of the United States Housing Act of 1937 where the request involves a project encumbered by a M2M or Demo Program lien.

**BACKGROUND**

This Notice replaces Housing Notice 2012-10, “Guidelines for Assumption, Subordination, or Assignment of Mark-to-Market (M2M) Loans in Transfer of Physical Assets (TPA) and Refinance Transactions” in its entirety and provides new instructions for the acquisition and/or refinancing of projects which have been through a M2M debt restructuring or a Demo Program restructuring (collectively, “Post M2M”) and are encumbered by HUD-held debt. In addition, Section 3 of this Notice replaces Appendix C of the Mark-to-Market Operating Procedures Guide regarding transfers of assets to qualified nonprofits. This Notice does not apply to transactions where the Post M2M debt will be repaid in full, although other HUD requirements and procedures may apply.

M2M allows HUD to restructure debt that is FHA-insured or Secretary-held on certain projects that have above-market project-based Section 8 contract rents. Through the M2M restructuring, HUD adjusts the rents down to market and the owner obtains a new first mortgage loan that is supportable at the new rents. In most M2M restructuring transactions, HUD pays off a portion of the existing FHA-insured or HUD-held formerly insured first mortgage through a one-time non-default payment of claim made on behalf of the owner. HUD documents the owner's continuing obligation to repay this amount through a Mortgage Restructuring Note ("MRN") and/or a Contingent Repayment Note ("CRN"). The Demo Program, a precursor to M2M, operated in much the same way, with the owner's obligation documented by one or more "Demo Notes." Except as otherwise specified, for the remainder of this Notice, the term "M2M" shall be used to mean either M2M or the Demo Program, and the term "Note" shall be used to mean an MRN, CRN, or Demo Note.

The repayment terms of the Notes include a "due on sale or refinance" clause. For an owner to transfer ownership of a project or refinance the new first mortgage lien debt without causing an acceleration of the subordinate debt evidenced by a Note, an owner must obtain a waiver of the due on sale or refinance clause from HUD. In the case of a transfer of ownership, if HUD grants the waiver, the new owner of the project would assume the obligations under the Note and HUD would agree to subordinate the mortgage securing the Note to a new first mortgage lien. This Notice governs HUD's review of such requests. Notwithstanding HUD's approval of a request to waive the due on sale or refinance clause in one instance, any future sale or refinance of the project remains subject to this Notice. In some instances, HUD also has authority to assign to a Qualified Nonprofit Purchaser (as defined herein) HUD's interest in, and right to receive subsequent payments on, an MRN Note and a CRN Note. This Notice also governs such assignments, ensuring that the proposed nonprofit assignee is qualified, and that the assignment benefits the current and future residents, the nonprofit, and HUD's interest in the long-term affordability of the project.

## **ORGANIZATION AND EXPLANATION OF MAJOR PROVISIONS**

This Notice includes the following Sections:

- Section 1 provides definitions for terms used in this Notice.
- Section 2 describes the processing requirements applicable to the activities covered by this Notice and governs any request to assume and/or subordinate M2M debt and to waive the due on sale or refinance clause contained in the loan documents that evidence and secure M2M debt.
- Section 3 governs any request made by a "Qualified Purchaser" (defined below) to receive certain types of debt relief with respect to an MRN or CRN. Section 3 does not apply to Demo Notes.
- Section 4 governs certain requests for a term extension of a Note.
- Section 5 governs any request for approval of a proposal under Section 8(bb)(1) of the United States Housing Act of 1937 for HUD to transfer the budget authority remaining on a project-based Section 8 Housing Assistance Payments (HAP) Contract at the time of its termination to another HAP Contract in cases where either the project from which budget authority is transferred (Project A) or the project to which it is transferred (Project B) is subject to a Full M2M Renewal Contract (defined below).

This Notice streamlines and revises pre-existing guidance related to the refinance, assumption, subordination, assignment, forgiveness, or modification of Notes. This Notice reduces processing requirements not warranted by the benefits and provides transparency regarding processing of requests not addressed in the prior guidance. Among the key provisions and changes are to:

- Streamline HUD review of the first mortgage debt to focus on maximizing Project cash flow, protecting long-term viability of the Project, and evaluating the impact on future valuation of the Project for the remaining term of the M2M Use Agreement.
- Emphasize preservation of the affordable housing resource as a core criterion for granting waivers of the due on sale or refinance clause.
- Replace the emphasis on “Strategic Communities” with an emphasis on preservation of affordable housing, as documented by meeting projected capital needs, as the basis for granting incentives within the Notice.
- Consolidate into this Notice the subjects covered in Appendix C of the Mark-to-Market Operating Procedures Guide and provide more detailed guidance regarding review of proposed Qualified Nonprofit Purchasers.
- Establish guidance on processing Notes that are in default to maximize coordination among HUD offices.
- Establish guidance on processing a request for approval of a proposal under Section 8(bb)(1) of the United States Housing Act of 1937 for HUD to transfer the budget authority remaining on a project-based Section 8 HAP Contract at Project A at the time of its termination to another contract (i.e., at Project B) when either project is subject to a Full M2M Renewal Contract.

### **EFFECTIVE DATE**

This Notice is effective immediately for all Requests or applicable transactions initiated after the date of publication of this Notice.

### **GUIDELINES FOR CERTAIN HUD APPROVALS REGARDING PROPERTIES ENCUMBERED BY HUD-HELD MARK-TO-MARKET PROGRAM DEBT AND PORTFOLIO REENGINEERING DEMONSTRATION PROGRAM DEBT**

**Section 1. Definitions.** Capitalized terms not otherwise defined shall have the meaning set forth below.

1.1. Acquiring organization or entity. For the purpose of Debt Relief, the term “acquiring organization or entity” means the legal entity that will acquire title to a Project (including fee simple, a ground leasehold interest, or some other form of title).

1.2. Affiliates. The term “Affiliate” means any entity that Controls another entity, is Controlled by another entity, or is under common Control with another entity.

1.3. Assignment. Transfer of an MRN and/or a CRN to a qualified nonprofit entity (see QNP). This process does not apply to Demo Notes.

1.4. Assumption. Transaction in which a Purchaser will assume a Seller's obligations under the loans evidenced by MRN, CRN, or Demo Note(s) and the Seller is released from such obligations.

1.5. Community Advisory Board or CAB. A CAB is a panel whose membership assures there will be significant representation of the views of the community in which the Project is located, and that has a substantive voice in Project operations as described in greater detail in Section 3.2(B)(b)(ii).

1.6. Control. The term "Control" shall have the more expansive of any meaning set forth in the applicable Notes and the meaning defined in 24 C.F.R. § 401.310(a)(2), as it may be amended from time to time, which, at the time of issuance of this Notice, reads:

*Control means the power to vote, directly or indirectly, 25 percent or more of any class of the voting stock of a company; the ability to direct in any manner the election of a majority of a company (or other entity's) directors or trustees; or the ability to exercise a controlling influence over the company or entity's management and policies. For purposes of this definition, a general partner of a limited partnership is presumed to be in control of that partnership.*

Further, a managing member of a limited liability company is presumed to be in control of that entity. HUD may make a similar presumption regarding the principal operating parties in other corporate structures not referenced in this Notice. In multilayered organizational structures, Control is not limited to a specific number of layers above the subject entity itself. The analysis of Control may disregard the separation of entities if HUD determines that such disregard is necessary to reflect how control is actually held and/or exercised.

1.7. CRN. A Contingent Repayment Note originated under M2M, secured by a mortgage that is usually in a third lien position encumbering a Project.

1.8. CRP. A Capital Recovery Payment, which is an incremental repayment of an Owner's required contribution toward M2M rehabilitation and transaction costs, with a market rate of return and subject to conditions specified in M2M legal documents, and which does not get transferred to a new Owner.

1.9. Debt Relief. The forgiveness, assignment, or Modification, as defined below, of an MRN and/or CRN, together with the security instruments that secures such Note(s), which HUD may provide in response to a QNP Request.

1.10. Demo Note. A note originated under the Demo Program, typically secured by mortgages in a second or third lien position encumbering a Project.

1.11. Demo Program. The Portfolio Reengineering Demonstration Program, first created in Section 210 of the Departments of Veterans Affairs and Housing and Urban Development and Independent Agencies Appropriations Act, 1996, P.L. 104-134.

1.12. Entity. A person, partnership, organization, business, or corporate entity that has a legal and separately identifiable existence.

1.13. Exception Rents. Above-market rents, as authorized under Section 514(g)(2) of MAHRA and as reflected in Exhibit A to the Full M2M Renewal Contract issued at closing upon completion of the M2M debt-restructuring process, which were established based on a Departmental determination that the housing needs of the tenants and the community could not be adequately addressed through a M2M debt-restructuring and Full M2M Renewal Contract based on comparable market rents.

1.14. Full M2M Renewal Contract. A HAP Contract originally issued under Section 8 of the United States Housing Act of 1937, and as renewed under Section 515 of MAHRA with a Full Mark-to-Market Renewal Contract or, if applicable, a Housing Assistance Payments Contract for Previous Mod Rehab Projects. As used in this Notice, this term does not include HAP contracts renewed with an Interim (Full) Mark-to-Market Renewal Contract or an Interim (Lite) Mark-to-Market Renewal Contract. When the procedures outlined in this Notice require the use of a new Full M2M Renewal Contract, Form HUD-9642 REV 03-15-2012, or its successor (or, if applicable, a new Housing Assistance Payments Contract for Previous Mod Rehab Projects, Form HUD-9644 REV 10/09, or its successor), must be used.

1.15. HAP Contract. A housing assistance payments contract, as authorized under Section 8 of the United States Housing Act of 1937 (including those renewed under MAHRA), between the contract administrator (HUD, or a public housing agency (PHA) acting under an annual contributions contract with HUD) and the owner. The contract administrator makes housing assistance payments to the owner in accordance with the HAP Contract.

1.16. High Priority Project. A High Priority Project shall be a Project where both of the following conditions are met:

- A) There is significant demand in the market for affordable housing units, as evidenced by a current market study. The market study must justify the projected absorption rate, lease-up period, and stabilized vacancy rate for the proposed development.
- B) There are significant physical, financial, or operational needs that HUD reasonably anticipates will be addressed by actions the Owner contracts with HUD to undertake within a reasonable period, which needs are evidenced by one or more of the following factors:
  - i) Functional obsolescence of the Project with respect to competing market demands, which obsolescence is demonstrated, and addressed or mitigated through the proposed transaction, to the satisfaction of HUD;
  - ii) A HUD-approved capital needs assessment demonstrates materially greater capital needs than can be addressed by the existing replacement reserve funds;
  - iii) The Project is either the transferring or receiving Project in a Section 8(bb) transfer pursuant to Section 5;
  - iv) Financial distress as evidenced by the Project's operational history such as underperformance or non-performance on the Notes, due to circumstances beyond Owner control;

- v) Ownership by an entity that is proposed to exit the ownership, capitalization, and operational structure, which entity is fully or partially debarred from future participation in HUD programs; or
- vi) Other evidence of physical, financial, or operational needs as determined by HUD.

1.17. Incentive Performance Fee or IPF. The Incentive Performance Fee is a percentage of annual effective gross income that the Owner may collect under certain conditions.<sup>1</sup>

1.18. Identity of Interest or IOI. Any relationship based on familial or other interpersonal ties or shared financial or other beneficial interests that would reasonably give rise to a presumption that the parties may not operate on an arms-length basis in establishing (a) the purchase price of the Project; (b) the cost of the design, rehabilitation, or construction; (c) the price for any service contracts; or (d) the terms of the financing. Relevant relationships include, without limitation, direct or indirect ownership interests (including officers, directors, shareholders, partners, trustees, managers, or members), financial interests (including employment, participation in hiring, or material contractual relationships), and familial relationships (including spouses, parents, grandparents, children, grandchildren, uncles, aunts, brothers, sisters, nieces, nephews, mothers-in-law, fathers-in-law, brothers-in-law, sisters-in-law, or the spouses or children of any of the foregoing). HUD may determine on a case-by-case basis that an IOI relationship exists whenever the facts and circumstances indicate that the parties in a transaction are not operating independently of such relationships.

1.19. MAHRA. The Multifamily Assisted Housing Reform and Affordability Act of 1997, Title V of the Departments of Veterans Affairs, Housing and Urban Development and Independent Agencies Appropriations Act, 1998 (Pub. L. No. 105-65, 111 STAT. 1384, approved 10/27/97, as amended), codified at 42 U.S.C. 1437f note, which established M2M (exclusive of the Demo Program).

1.20. Market Rents. Rents based on comparable market rents, as authorized under Section 514(g)(1) of MAHRA, and as reflected in Exhibit A to the Full M2M Renewal Contract issued at closing upon completion of the M2M debt-restructuring process.

1.21. Mark-to-Market Program or M2M. The Multifamily Housing Mortgage and Housing Assistance Restructuring (Mark-to-Market) Program established pursuant to MAHRA and implementing regulations at 24 C.F.R. §§ 401 and 402.

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<sup>1</sup> The conditions under which the Incentive Performance Fee may be collected are set forth in the applicable transaction's M2M regulatory agreement.

1.22. Mark-to-Market Operating Procedures Guide. The Mark-to-Market guidelines and processing tools for the statutory and regulatory requirements and HUD's expectations, standards, and requirements to be followed in the review and processing of Projects in M2M. The guide can be found at:

[https://www.hud.gov/program\\_offices/housing/mfh/presrv/presmfh/opglinks](https://www.hud.gov/program_offices/housing/mfh/presrv/presmfh/opglinks)

1.23. Mark-to-Market (M2M) Use Agreement. A recorded use agreement on a form prescribed by HUD with a minimum term of 30 years, as required under Section 514(e)(6) of MAHRA, for Projects that undergo M2M debt-restructuring and whose Section 8 HAP Contract is renewed as a result with a Full M2M Renewal Contract.

1.24. Modification. The term "Modification" refers specifically to certain changes to MAHRA-required provisions in a Note excluding certain minor amendments to loan documents. Minor amendments include items such as those that (a) evidence the change in responsible parties associated with any assumption, subordination, or assignment under this Notice; (b) eliminate the CRP (when a CRP is present); and/or (c) extend the maturity date to make it coterminous with a new first mortgage loan, if appropriate.

1.25. MRN. A Mortgage Restructuring Note originated under M2M that is secured by a mortgage that is usually in a second lien position encumbering a Project.

1.26. Multifamily Regional Center. One of the regional offices with asset management supervisory authority within the Office of Multifamily Housing Programs, Office of Housing, in the U.S. Department of Housing and Urban Development, or its successor office.

1.27. Net Proceeds. Proceeds as defined in Section 1.32 reduced by any usual and customary expenses of the proposed transaction approved by HUD and paid at the closing of the proposed transaction. Usual and customary expenses of the proposed transaction typically include third-party brokerage fees, local and state transfer taxes, legal and title fees, and other costs of the sale or purchase of the Project. Usual and customary expenses for this purpose generally exclude, however, Project payables and IOI payments.

1.28. Note. Any of a MRN, a CRN, or a Demo Note.

1.29. OAMPO. The Office of Asset Management and Portfolio Oversight, within the Office of Multifamily Housing Programs, Office of Housing, in the U.S. Department of Housing and Urban Development, or its successor office.

1.30. Owner. The term "Owner" has the same meaning as in Section 516(a) of MAHRA, which reads in relevant part: "[t]he term 'owner' as used in this subsection, in addition to it having the same meaning as in Section 8(f) of the United States Housing Act of 1937, also means an affiliate of the owner." The term "Owner" can refer to the entity either before or after the sale or transfer associated with a Request.

1.31. Pay-Down. The payment described in Section 2.4(I) of this Notice. The purpose of the Pay-Down is to reduce the outstanding balance of the Notes when the transaction proposed involves Proceeds that will benefit the Seller or Purchaser. The Pay-Down represents recovery of a portion of the value created through the M2M debt restructuring.

1.32. Proceeds. All cash, fees, and other consideration paid to or on behalf of the Seller, Purchaser, or IOI entities of either the Seller or Purchaser. Proceeds include, without limitation, developer and other fees, deferred payments, Project accounts (including, without limitation, operating reserves, replacement reserves, tax and insurance escrows, and security deposit accounts), allocations of accounts payable, or other reductions in the party's liabilities, whether paid as part of a transaction or following closing of a transaction. Proceeds also include any indemnification to either party of a Pay-Down amount by the other party. Proceeds do not include distributions of Surplus Cash or payment of the CRP or IPF. The treatment of Proceeds in this Notice varies based on whether the Proceeds are received by the Seller or Purchaser.

1.33. Program Obligations. "Program Obligations" means (a) all applicable statutes and any regulations issued by the Secretary pursuant thereto that apply to the Project, including all amendments to such statutes and regulations, as they become effective, except that changes subject to notice and comment rulemaking shall become effective only upon completion of the rulemaking process, and (b) all current requirements in HUD handbooks and guides, notices, and mortgagee letters that apply to the Project, and all future updates, changes and amendments thereto, as they become effective, except that changes subject to notice and comment rulemaking shall become effective only upon completion of the rulemaking process, and provided that such future updates, changes and amendments shall be applicable to the Project only to the extent that they interpret, clarify and implement terms of the Project's contractual agreements with HUD rather than add or delete provisions from such documents.<sup>2</sup>

1.34. Project. A multifamily housing property for which a Request is made and that is encumbered by a mortgage securing a Note or is subject to a Full M2M Renewal Contract.

1.35. Purchaser. The legal entity that is proposed to own the Project, together with any of its Affiliates. The term "Purchaser" is used to distinguish the Owner after the sale or transfer from the Owner prior to the sale or transfer.

1.36. Qualified Nonprofit Purchaser or QNP. The acquiring entity eligible for Debt Relief upon Purchase of the Project pursuant to and as defined in more detail in Section 3. The acquiring entity must be a nonprofit entity, a nonprofit entity's directly and exclusively controlled Affiliate(s), a public agency, or a tenant organization. A QNP includes a Priority Purchaser under 24 C.F.R. § 401.2.

1.37. QNP Request. A request for HUD's approval as a Qualified Nonprofit Purchaser and for Debt Relief, made in conjunction with a Request.

1.38. RCS. A Rent Comparability Study conducted in accordance with Chapter Nine of the Section 8 Renewal Guide.<sup>3</sup>

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<sup>2</sup> Handbooks, guides, notices, and mortgagee letters are available on HUD's official website (<http://www.hud.gov/offices/adm/hudclips/index.cfm>, or a successor location to that site).

<sup>3</sup> [https://www.hud.gov/sites/documents/508FIN\\_CONSOL\\_GUIDE6\\_8\\_17.PDF](https://www.hud.gov/sites/documents/508FIN_CONSOL_GUIDE6_8_17.PDF)



1.39. Recap. The Office of Recapitalization, within the Office of Multifamily Housing Programs, Office of Housing, in the U.S. Department of Housing and Urban Development, or its successor office.

1.40. Refinance. A transaction involving the payoff of the existing first mortgage loan with funds from a new first mortgage loan from either a new lender or the existing lender, whether or not the transaction would increase the outstanding principal amount of the debt. A Refinance does not involve any change in ownership.

1.41. Request. A request (a) for HUD to waive the “due on sale or refinancing” clause in a Note and allow the Assumption and/or Subordination of such Note, or, in the case of a QNP Request, provide Debt Relief in connection with an acquisition of title; or (b) for HUD to approve a proposed transfer of budget authority under Section 8(bb)(1) of the United States Housing Act of 1937 and Section 5 of this Notice.

1.42. Return to Owner. The “Return to Owner” is defined in Chapter 3 of the Mark-to-Market Operating Procedures Guide and includes the Capital Recovery Payment (CRP), the Incentive Performance Fee (IPF), and the cash flow split with HUD pursuant to the Notes.

1.43. Section 8. Section 8 of the United States Housing Act of 1937 (42 U.S.C. § 1437f).

1.44. Section 8(bb). A provision in the United States Housing Act of 1937 that requires HUD (under Section 8(bb)(1)) to transfer to another HAP Contract any budget authority remaining on a project-based Section 8 Housing Assistance Payments Contract at the time of its termination under terms prescribed by the Secretary. 42 U.S.C. § 1437f(bb)(1).

1.45. Section 8(bb) Notice. Housing Notice 2015-03, or any successor notice, together with any other guidance applicable to Section 8(bb) (e.g., published responses to frequently asked questions).<sup>4</sup>

1.46. Section 8(bb) Units. Housing units supported by budget authority transferred to a new site pursuant to Section 8(bb), and thus increasing the number of units receiving rental assistance at the new site.

1.47. Seller. The Owner of the Project together with any of its Affiliates. The term Seller is used in the Transfer context to distinguish the Owner prior to the sale or transfer from the Owner after the sale or transfer.

1.48. Subordination. A transaction in which the lien securing a Note will be subordinated to a new mortgage lien.

1.49. Surplus Cash. Cash determined by the Multifamily Regional Center to be remaining at the end of each fiscal year from the operations of a Project in accordance with the documents

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<sup>4</sup> Housing Notice 2015-03 can be found at <https://www.hud.gov/sites/documents/15-03HSGN.PDF>.

that evidence, secure, or are executed with a Note. In the case of a Demo Note, Surplus Cash as used herein shall refer to “Net Cash” as defined in the Demo Note.

1.50. Transfer. Transfer shall mean the sale or transfer of a Project or any portion thereof, an interest in the Owner, or an interest in an entity with Control of the Owner. The analysis of a transfer may examine multi-step transfers as a whole if HUD determines that such integrated review is necessary to reflect how ownership is actually held.<sup>5</sup>

1.51. Transfer of Physical Assets or TPA. A Transfer where the FHA-insured first mortgage survives after the Project is acquired by the Purchaser. “TPA” also refers to the process through which HUD reviews such Transfers.

## **Section 2. Submission and Processing of Requests for Waiver of the Due on Sale or Refinance Clause**

2.1. Initiation of Requests. The necessary documentation to initiate all Requests, including QNP Requests seeking Debt Relief, must be submitted to the Project’s applicable Multifamily Regional Center. A courtesy copy of the Request may be submitted to Recap simultaneously if the Request is subject to Recap review based on the criteria listed below in Section 2.2. A courtesy copy submission to Recap may be particularly beneficial to the Purchaser in managing deadlines associated with the proposed transaction. Requests which are part of a portfolio of simultaneous transactions should identify the other related transactions. All submission requirements and instructions for Requests, including a *Draft Applicants’ Checklist: Request for Waiver of M2M “Due on Sale or Refinancing” Clause*, can be found online at [https://portal.hud.gov/hudportal/HUD?src=/program\\_offices/housing/mfh/presrv/presmfh/about\\_m2m](https://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/mfh/presrv/presmfh/about_m2m). The public may submit transaction-specific questions regarding submission requirements and instructions to [PostM2M@hud.gov](mailto:PostM2M@hud.gov).

2.2. Processing of Requests. Requests submitted to the Multifamily Regional Center which meet any of the criteria set forth in Section 2.2 A) through G) below, shall be routed to Recap for processing. The applicable Multifamily Regional Center shall process and close all other Requests without Recap approval consistent with existing Recap guidance to the Multifamily Regional Centers, as such guidance may be amended or replaced by Recap from time to time.

- A) All Assumptions and Subordinations involving Proceeds to Seller or Purchaser;
- B) All Assumptions and Subordinations involving Modifications to an existing Note;
- C) All Refinances of the existing first mortgage if such Refinance increases the debt service payment, increases the unpaid principal balance by an amount greater than the loan fees and transaction costs (such as title and recording) directly attributable to the Refinance, or extends the term of the existing loan;

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<sup>5</sup> Transfers which do not involve a TPA are sometimes referred to as “assignments of the HAP.”

- D) All Refinance transactions combined with changes to the Project ownership at any level;
- E) All Requests that are part of the Transfer of a portfolio of Projects between a Seller and a Purchaser if any of the Requests within the portfolio are subject to processing by Recap;
- F) All QNP Requests for Debt Relief; and
- G) All Requests which involve a transfer of budget authority to or from the Project pursuant to Section 8(bb).

2.3. Basic Eligibility for Waiver. To be eligible for a waiver of the due on sale or refinance clause(s) in a Note or other documents securing or evidencing a Note, Purchasers and Owners must also meet the following criteria, as applicable:

- A) If the Request is in connection with a TPA or other Transfer, the Purchaser must:
  - i) Have all elements of the TPA or other Transfer other than the Request reviewed by the applicable Multifamily Regional Center under HUD's applicable requirements;
  - ii) Not have any outstanding violations of fair housing laws in connection with any Project owned by the Purchaser, unless otherwise approved by HUD's Office of Fair Housing and Equal Opportunity. This includes, but is not limited to, an outstanding unresolved Fair Housing Act charge and/or an outstanding unresolved court finding of violation of the Fair Housing Act, Title VI of the Civil Rights Act of 1964, Section 504 of the Rehabilitation Act of 1973, or the Americans with Disabilities Act (ADA);
  - iii) Set forth a plan acceptable to HUD to cure any current non-compliance with Program Obligations and any defaults (or events which, with the giving of notice and/or passage of time, would become a default) under a Note or any document that further evidences, secures, or was executed contemporaneously with the Note; and
  - iv) Be eligible in a manner consistent with the M2M debt restructuring eligibility criteria set forth in MAHRA.
- B) If the Request is in connection with a Refinance, the Owner must:
  - i) Not have any outstanding violations of fair housing laws in connection with any Project owned by the Owner, unless otherwise approved by HUD's Office of Fair Housing and Equal Opportunity. This includes, but is not limited to, an outstanding unresolved Fair Housing Act charge and/or an outstanding unresolved court finding of violation of the Fair Housing Act, Title VI of the Civil Rights Act of 1964, Section 504 of the Rehabilitation Act of 1973, or the Americans with Disabilities Act (ADA).
  - ii) Be in full compliance with Program Obligations and have no defaults (or events which, with the giving of notice and/or passage of time, would become a default) under a Note or any document that further evidences, secures, or was executed contemporaneously with the Note.

## 2.4. Review Requirements.

- A) TPAs or Other Transfers. All TPAs and Transfers where the Note remains outstanding are subject to approval under this Notice. Review pursuant to this Notice is in addition to, and does not replace or substitute for, any other review required under HUD guidance, such as reviews of a TPA or an assignment of a HAP Contract. HUD review shall encompass properties not encumbered by the M2M Use Agreement to the extent such properties are anticipated to be under common ownership with the Project. For Requests approved by Recap, Recap will advise the Multifamily Regional Center of Recap's approval, rejection, or modification of the Request, together with any conditions associated with Recap's determination. TPAs or other Transfers will be processed by the Multifamily Regional Center according to their established procedures.<sup>6</sup> A Purchaser must affirmatively assume the Notes as part of a TPA or Transfer. No Project may be sold "subject to" such encumbrance(s) and absent an affirmative assumption of the Notes.
- B) Outstanding Surplus Cash Note(s) Payments from Prior Fiscal Years. Upon receipt of a Request, the reviewing office (either the Multifamily Regional Center or Recap) will confirm whether HUD has received all Surplus Cash payments due on Note(s) for all completed fiscal years. The Owner must remit all outstanding Surplus Cash payments due to HUD in consideration of the Request.
- C) Anticipated Note(s) Payments for the Partial, Current Fiscal Year. A partial year audit or un-audited financial statement certified by the Seller shall be submitted to HUD following the closing of a Transfer, covering the period through the date of the closing. The audit, financial statement or in-house financial statements shall calculate any required partial-year Surplus Cash payment on the Note(s) for the current year owed to HUD. The Seller and the Purchaser shall be jointly and severally liable for payment of such amount to HUD. It shall be the responsibility of the Seller and the Purchaser to determine both the method and the responsible party by which the payment is remitted to HUD. For all Demo Notes, the partial year audit or financial statement must calculate the partial year payment based on the specific payment terms of the Note(s).
- D) Project Accounts in a Sale Transaction.
  - i) HUD shall require the Seller to transfer to the Purchaser for the benefit of the Project the following amounts for their designated purposes:
    - a) The replacement reserve account funded at the lesser of 1) the amount necessary to satisfy HUD requirements and other affordable housing

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<sup>6</sup> For FHA-insured loans, such procedures include collection of a TPA transfer fee in accordance with 24 C.F.R. § 200.40(h).

- regulatory restrictions in place prior to the Transfer which will continue after the Transfer, or 2) the current account balance;
- b) Any operating reserve account funded at the lesser of 1) the amount necessary to satisfy HUD requirements and other affordable housing regulatory restrictions in place prior to the Transfer which will continue after the Transfer, or 2) the current account balance;
  - c) The balance in the tax and insurance escrows, unless a lesser amount is approved by HUD to align with a new lender's estimate of the tax and insurance escrow needs if the first mortgage is refinanced; and
  - d) The security deposit account funded to correspond with the contractual security deposits for all occupied units.
- ii) The Seller and the Purchaser may dispose of the cash in the specific accounts according to their negotiated business relationship by crediting and debiting amounts from the purchase price. However, if the net effect is that the Seller retains the value of any of the forgoing Project account balances, HUD will treat such funds as Proceeds to the Seller.
  - iii) The Purchaser is required to reestablish and fund all such accounts in an amount equal to the greater of the requirements of the first mortgage lender and the Multifamily Regional Center.
- E) Elimination of Capital Recovery Payments. As a condition of HUD's approval to waive the due on sale provision and allow an Assumption and Subordination, the Purchaser shall agree to eliminate the CRP as an eligible Project expense.
- F) M2M Rehabilitation. If the Owner has not completed the rehabilitation work agreed upon in the M2M transaction, as identified by Recap, prior to closing the Owner shall either:
- i) Complete the work to the satisfaction of Recap; or
  - ii) Transfer the remaining balance of the rehabilitation escrow to the Purchaser, and the Purchaser must provide a proposed rehabilitation plan acceptable to Recap incorporating any incremental cost as part of the Request.
- G) Lien Position. HUD shall require that the lien(s) of the Note(s) be senior to any other debt payable from cash flow or with contingent payment terms. The Note(s) may be subordinated to any HUD-approved amortizing, non-contingent, first-mortgage-lien debt.
- H) Financial Viability. For any Request reviewed by Recap pursuant to Section 2.2, the Project must be financially viable. Compliance with all of the following shall be an indication of financial viability, although HUD may also consider alternative measures of financial viability proposed by the Owner:
- i) The projected debt service coverage on any new permanent first mortgage loan as shown in a HUD-approved operating pro forma shall either (a) be equal to or greater than 1.20, or (b) be approved in a firm commitment for FHA-insured financing.

- ii) The permanent first mortgage loan must have a fixed rate of interest. There shall be no adjustable-rate loans during the term of the Note(s).
- iii) The permanent first mortgage loan must have a term equal to or greater than the least of (a) 15 years and (b) the remaining term of the M2M Use Agreement.
- iv) The permanent first mortgage loan payments must be sized to fully amortize the debt over a period of 40 years or less. A balloon payment is permitted if the mortgage term is shorter than the amortization period.
- v) The Request must demonstrate to HUD's satisfaction that the proposed operating expense levels are adequate to maintain the property's operations and physical condition for the remaining term of the M2M Use Agreement.
- vi) The estimated value of the Project, as determined by HUD based on the Project's estimated net operating income at the earlier of the expiration of the term of the proposed new permanent first mortgage or of the proposed M2M Use Agreement, must be equal to or greater than the estimated outstanding balance of the HUD debt, including principal and interest.
- vii) The proposed replacement reserve deposits, operating accounts, and vacancy estimates must be approved by the Multifamily Regional Center prior to a transaction being approved for closing.

I) Pay-Down.

- i) For any Request reviewed by Recap pursuant to Section 2.2 of this Notice, HUD will condition approval of the Request upon payment to HUD of a Pay-Down. The Pay-Down shall equal the greater of:
  - a) One-half of the Net Proceeds to be paid to the Seller; or
  - b) One-third of the sum of the Net Proceeds to be paid, accrued, or realized by the Seller and by the Purchaser.
- ii) As stated in Section 1.32, Proceeds received by a party include any indemnification or reimbursement to such party of a Pay-Down amount by the other party.

J) Identity of Interest Operating Contracts. For any Request reviewed by Recap pursuant to Section 2.2 of this Notice, HUD will require the disclosure of operating contracts and other contracts that will be established or survive after the closing of the Transfer or Refinance in which there is an IOI with either the Seller or Purchaser, or any relationship based on familial or other interpersonal ties or shared financial or other beneficial interests that would reasonably give rise to a presumption that the parties may not operate on an arms-length basis in establishing the price for any service contracts, including employment, participation in hiring, or material contractual relationships.

- K) Preservation of Affordability. For any Request reviewed by Recap pursuant to Section 2.2 of this Notice:
- i) For Projects without Exception Rents, to facilitate the refinancing of a Project's first mortgage loan and satisfy a typical lender condition for such refinancing, Owners may request an extension of the term of the Project's Full M2M Renewal Contract. HUD shall grant such requests only if the Owner agrees to an extension of the term of the Use Agreement, if necessary, to equal the term of the renewed Full M2M Renewal HAP Contract.
  - ii) For Projects with Exception Rents, except as required in Section 3.4(E), the term of the M2M Use Agreement may not be extended beyond its current term which may, in some cases, restrict the term of a new Full M2M Renewal Contract to a period of less than 20 years. Except for transactions with QNPs which have a M2M Use Agreement for more than 30 years, any subsequent Full M2M Renewal Contract for the period after the expiration of the term of the M2M Use Agreement will be under then-applicable statutes and regulations, using any available HAP Contract renewal option for which the Project is eligible at that time.
- L) High Priority Projects. For any Request reviewed by Recap pursuant to Section 2.2 of this Notice, HUD will eliminate the proposed developer fee<sup>7</sup> from the calculation of Proceeds if the Project is a High Priority Project and if the Owner or Purchaser demonstrates that sufficient funds will be available to meet the 20-year capital needs of the Project as documented by a HUD-approved Capital Needs Assessment (CNA).<sup>8</sup> The Owner or Purchaser must demonstrate the availability of funds through the initial funding of the replacement reserve account, through annual deposits to the replacement reserve account, or through other measures acceptable to HUD.
- M) Valuation Analysis of the Modification. For any Request reviewed by Recap pursuant to Section 2.2 which does not involve a QNP Request, any Note amendment which extends the maturity date of the Note or is reasonably

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<sup>7</sup> Developer fees may be paid only with capital sources reflected in a HUD-approved sources and uses or with the Return to Owner.

<sup>8</sup> The Capital Needs Assessment (CNA) e-Tool automates and standardizes the preparation, submission and review of a capital needs assessment. The CNA e-Tool format is expected only with Requests seeking designation as High Priority Projects and only if required by other Office of Multifamily Housing Program guidance. For example, if the CNA e-Tool is required for asset management of M2M and Post-M2M projects, then the CNA e-Tool must be used in connection with a Request for a High Priority Project. If the Request involves FHA-insured financing and the CNA e-Tool is required for underwriting of FHA-insured multifamily projects, then the CNA e-Tool must be used in connection with such Request. See: [https://www.hud.gov/program\\_offices/housing/mfh/CNA](https://www.hud.gov/program_offices/housing/mfh/CNA) for more information. In all other situations, the CNA e-Tool is not required but the CNA must be in a form acceptable to HUD.